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Robert H. Allphin
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1954 Kentucky Tax Legislation

By ROBERT H. ALLPHIN*

The 1954 Regular Session of the General Assembly of the Commonwealth of Kentucky enacted a voluminous amount of legislation pertaining to revenue and taxation. It is the purpose of this article to briefly review the more important tax legislation, placing particular emphasis on legislation pertaining to income taxes. In treating this subject the legislation will be divided into four categories: Excise Taxes, Property Taxes, Inheritance Taxes, and Income Taxes.

I. EXCISE TAXES

H. B. 17 amends KRS 243.720 by increasing the consumption tax on wine to 50 cents per gallon and the consumption tax on malt beverages to \$2.50 per 31 gallon barrel, with a proportionate rate on both wine and malt beverages sold in smaller containers.

H. B. 18 amends KRS 138.510 by levying a pari-mutuel tax of four percent on the first eighteen millions of dollars wagered during the year and six percent on amounts wagered in excess of eighteen million dollars. It also repealed KRS 138.520, the statute exempting pari-mutuel betting at Keeneland from the pari-mutuel tax.

H. B. 19 amends KRS 138.140 (1) by taxing cigarettes at the flat rate of three cents per pack of twenty or fraction thereof. The prior law taxed cigarettes at a sliding rate according to price.

H. B. 17 imposes a gasoline usage tax of seven cents per gallon on gasoline purchased without the state and consumed within the state by motor vehicles having a gross weight of not less than eighteen thousand pounds. This bill was designed to plug a loophole in the prior gasoline tax law whereby motor carriers were purchasing gasoline without Kentucky and consuming such gasoline on Kentucky's highways without payment of the gasoline excise tax.

* Commissioner of Revenue, Commonwealth of Kentucky. A.B., LL.B., University of Kentucky.

H. B. 201 liberalizes the admission tax exception by amending KRS 138.020 (5) to provide that the tax shall not apply to admissions to entertainment presented by non-profit civic, fraternal, charitable, musical, social or educational clubs or associations if no professional entertainers are employed and all net profits are used for civic, charitable, religious or educational purposes within Kentucky. In the event professional entertainers are employed the exemption does not apply, unless at least 75 percent of the gross proceeds from admissions are used for charitable, religious or educational purposes within Kentucky.

H. B. 428 amends KRS 138.344 by extending from 120 days to 180 days the period during which an application for refund of excise taxes paid on gasoline used for agricultural purposes may be filed with the Department of Revenue.

II. GENERAL PROPERTY TAXES

H. B. 202 authorizes the Department of Revenue to assess intangible property omitted from property taxation whenever the owner refuses to voluntarily list such property for taxation. Prior to the effective date of H. B. 202, if a taxpayer refused to list intangibles voluntarily the Department of Revenue was required to file an omitted tax statement in the county court of the taxpayer's residence.

H. B. 204 amends KRS 136.120 and KRS 136.160 (3) to include in the franchise taxpayer classification for property tax purposes, common carrier water transportation companies. It also creates two new sections of KRS (136.181 and 136.182) authorizing the Department of Revenue to assess and allocate among the local taxing districts contract and private water craft plying routes within and without Kentucky and owned by non-resident persons.

III. INHERITANCE TAXES

KRS 140.030 as presently constituted permits a tax-free transfer of the first twenty thousand dollars of life insurance payable to a designated beneficiary, other than the insured's estate. If the value of proceeds payable to designated beneficiaries exceeds twenty thousand dollars, the exemption is pro-rated among the designated beneficiaries. Effective July 1, 1956, all insurance pro-

ceeds becoming payable to designated beneficiaries will be exempt from inheritance and estate taxes.

Prior to the effective date of S. B. 190, transfers of property to charitable, educational or religious institutions and transfers for charitable, educational or religious purposes were exempt from inheritance and estate taxes only if the amounts so transferred were to be employed for charitable, educational or religious purposes within Kentucky. However, if the amounts were to be expended in some other state that did not tax transfers to be used for charitable, educational or religious purposes within Kentucky, the exemption was allowed. S. B. 190 amends KRS 140.060 by deleting the reciprocity provision. Effective with respect to estates of decedents dying on or after June 17, 1954, all transfers for charitable, educational or religious purposes are exempt from taxation even though they may be expended outside Kentucky.

IV. INCOME TAXES

The most extensive and important single piece of legislation enacted by the 1954 Regular Session is H. B. 21. It completely revises the individual, fiduciary and corporation income tax laws and implements a "pay-as-you-go" method of collection modeled after the Federal withholding and estimated tax collection system.

Space limitations prevent complete discussion of all the changes, and more salient amendments will be briefly outlined.

It should be noted that one of the prime objectives of House Bill 21 was to conform, as far as possible, the concept of net income with the concept of net income contained in the Revenue Code of 1939. This was accomplished, but much of the ground gained was lost through enactment of the Revenue Code of 1954¹ by the 83rd Congress.

A. *Individual Income Taxes*

1. *Dependency tax credits*—The new law adopts the Federal definition of dependent and changes the old law by permitting additional ten dollar tax credits for dependents over 18 years of age, taxpayers over 65 years of age or blind, and a taxpayer's spouse who is over 65 years of age or blind. The credits allowed

¹ H.R. 8300.

to a spouse over 65 or blind are applicable only in cases where a joint return is filed.²

2. *Capital gains and losses*—The prior law³ arbitrarily divided the tax treatment of gains and losses from sales or exchanges of capital assets at two years. If the gain or loss resulted from disposition of an asset held less than two years, the gain or loss was fully taken into account. If the asset disposed of was held more than two years, the gain or loss was completely excluded from the computation of net income. There was also no provision permitting a capital loss carry-over.

The new law repeals KRS 141.100 and adopts the Federal definition of net income.⁴ These changes, in effect, adopt the Federal treatment of capital gains and losses, except that the alternative tax computation is not permitted. One-half of a long-term gain is included in net income and the excess of capital losses over capital gains may be carried forward in the same manner they are carried forward for Federal tax purposes.

3. *Non-business deductions*—Of particular interest to top-bracket taxpayers is the fact that through adoption of the Federal definition of net income a non-business deduction of Kentucky income taxes paid or accrued will be permitted. This will be of substantial tax benefit to any individual who pays several thousands of dollars of Kentucky income taxes each year. In addition, other miscellaneous taxes deductible for Federal purposes, but not in computing Kentucky net income, are now allowable deductions. The amounts deductible for charitable contributions are increased through use of the Federal definition of net income in determining the maximum limit of the deduction. Under the pre-'54 law, the maximum limitation was determined by reference to the Kentucky adjusted gross income; an amount that was usually less than Federal adjusted gross income.

B. *Trusts and Estates*

The tax treatment accorded trusts and estates has been completely revised to conform same to the treatment obtained under

² KY. REV. STAT. 141.060.

³ KY. REV. STAT. 141.100.

⁴ KY. REV. STAT. 141.010 (a).

the Revenue Code of 1939. Because of space limitations these changes cannot be reviewed in this article. Suffice it to say that, with the exception of the Federal income tax deduction and certain exempt items of income, the computations of net incomes of trusts and estates and the beneficiaries' shares of income are made identical with the Federal computations.

Formerly, an estate or trust was not permitted a tax credit. The new law allows a twelve dollar tax credit to an estate and a two dollar tax credit to a trust. This change was made in order to relieve smaller estates and trusts not required to file Federal returns from the duty of filing Kentucky returns.

C. Corporations

The three major changes made in the corporate income tax statutes concern treatment of gains and losses, proration of the Federal income tax deduction and the determination of Kentucky net income resulting from the operations of related taxpayers.

1. *Gains and losses*—The pre-'54 law took all gains and losses resulting from the sale or exchange of capital assets held less than two years fully into account. Conversely, gains and losses from disposition of capital assets held more than two years were ignored.

The new law requires all gains from sale or exchange of capital assets to be taken fully into account, regardless of the holding period. Long-term losses may be carried forward in the same manner they are carried forward for Federal tax purposes and so-called 117(j) losses may be offset against ordinary income.

2. *Pro-ration of Federal income taxes*—The Court of Appeals in *Clayton & Lambert Mfg. Co. v. Kentucky Tax Commission*,⁵ permitted a corporation to deduct Federal income tax accrued as the result of a non-taxable gain realized from the sale of capital assets situated outside of Kentucky. The new law specifically prohibits the deduction of Federal income taxes paid or accrued on income not subject to taxation under Chapter 141.⁶

3. *Tax treatment of affiliated taxpayers*—The prior law contained no specific provision for determining the net income attributable to Kentucky in the case of a controlled corporation. As a result, many tax authorities were of the opinion that the De-

⁵ 265 S. W. 2d 449 (1953).

⁶ KY. REV. STAT. 141.120 (6).

partment of Revenue did not possess the authority to require the filing of consolidated returns or to allocate items of income and deductions among the members of the related group. The new law specifically confers such authority on the Department and also authorizes the Department to assess the resulting tax liability against any one or more of the members of the related group.

D. *Withholding and Estimated Tax Withholding*

Beginning July 1, 1954, all employers subject to the jurisdiction of Kentucky are required to withhold a tax from wages paid employees resident of Kentucky and non-resident employees performing services in Kentucky, determined as prescribed in KRS 141.360. The amounts withheld during a full calendar year period from the wages of a particular employee will usually approximate such employee's final income tax liability. The definitions and administrative provisions are conformed as closely as possible to Federal definitions and administrative provisions. However, unlike the Federal law, additional withholding exemptions are not permitted a taxpayer who is over 65 years of age or blind or a taxpayer's spouse who is over 65 or blind. This deviation was necessary in order to avoid undue complexity in the withholding tables.

Estimated Tax—An individual having a gross income of \$1500 or more, at least \$1000 of which is from sources other than wages subject to withholding, is required to file a declaration of estimated tax and pay the estimated tax in installments. The provisions⁷ are modeled after their Federal counterparts and, of course, are mainly directed to the self-employed. The key dates are April 15, July 15, and November 15, and the tax, general speaking, will be paid in three equal installments on those three dates. For the tax year 1954, the declaration is due November 15, 1954, and one-half of the estimated tax must be paid at that time.

Corporations are not subject to the estimated tax provisions. However, it should be pointed out that corporate taxes due for taxable years beginning on or after January 1, 1954, must be paid in full on or before the due date of the return. Under the old law, corporations were permitted to pay their taxes in three equal installments.

⁷ KY. REV. STAT. 141.300, *et seq.*